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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION TWO

BKM TOTAL OFFICE OF CALIFORNIA et al., Plaintiffs and Respondents, v. PACIFIC INSURANCE CO., LTD., et al., Defendants and Appellants.	B173973 (Los Angeles County Super. Ct. No. BC303125)

APPEAL from an order of the Superior Court of Los Angeles County. Aurelio Munoz, Judge. Affirmed.

Ropers, Majeski, Kohn & Bentley, Todd A. Roberts and Terry Anastassiou for Defendants and Appellants.

Girardi & Keese and Thomas V. Girardi; Corbett, Steelman & Specter and Richard B. Specter for Plaintiffs and Respondents.

* * * * * *

Defendants Pacific Insurance Company, Ltd. (Pacific) and First State Management Group, Inc. (First State) appeal an order denying their motion to compel arbitration pursuant to Civil Code section 2860, subdivision (c). (All statutory references are to the California Civil Code unless otherwise indicated.) Because we find this case does not involve a dispute over the amount billed or the billing rates of independent (*Cumis*)[1] counsel, we conclude the matter is not subject to arbitration, and we affirm.

FACTUAL AND PROCEDURAL BACKGROUND

The Allegations of the Complaint.

In their complaint filed in this action respondents alleged the following facts in support of causes of action for breach of the implied covenant of good faith and fair dealing, breach of contract, intentional misrepresentation, negligent misrepresentation, breach of duty to defend, breach of fiduciary duty, breach of statutory duty, and conspiracy:

Pacific issued an Employment Practices Liability insurance policy (the "Policy") to plaintiffs[2] for the term from August 2, 1999 to August 2, 2000.

In June 2000, respondents tendered a lawsuit, entitled *Dacrey Northrup v. BKM Total Office of California et al.*[3] (the "*Dacrey Northrup* action"), to appellants for defense and indemnification under the Policy. Although First State ultimately accepted the defense of the *Dacrey Northrup* action without a reservation of rights, appellants delayed responding to the tender until after the responsive pleading was due, forcing

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1 *San Diego Federal Credit Union v. Cumis Ins. Society, Inc.* (1984) 162 Cal.App.3d 358 (*Cumis*).

2 Plaintiffs are BKM Enterprises, Inc., BKM Total Office of California, and BKM Total Office of California, L.P. (collectively respondents).

3 Los Angeles Superior Court case No. BC232300.

respondents to retain their own counsel to defend the action. Thereafter, in accepting the defense and indemnification of the *Dacrey Northrup* action, First State required compliance with their own guidelines, which required advance authorization for virtually every activity an attorney might undertake in conducting a defense. But despite respondents' best efforts to comply with the guidelines, appellants did not respond to requests for authorization, refused for over a year to pay any legal fees incurred for respondents' defense, and otherwise failed to defend respondents' interests as required under the provisions of the Policy.

Settlement discussions in the *Dacrey Northrup* action took place in July 2001. At that time, appellants acknowledged that no reservation of rights had previously been issued, but in the face of a settlement demand approaching policy limits, appellants informed respondents of their intent to issue a reservation of rights letter as well as to consult coverage counsel concerning coverage issues regarding claims they viewed as outside the terms of the Policy. Appellants then responded to a settlement demand within policy limits by agreeing to pay only a portion of the settlement and insisting that respondents pay the rest. Respondents refused appellants' demand.

In August 2001 appellants interviewed certain present and former employees of BKM Total Office of California, with respect to the allegations in the *Dacrey Northrup* action. Prior to the interviews, respondents specifically requested that one former employee not be contacted, warning that contact could result in this employee filing her own complaint against respondents. Appellants disregarded the request, interviewed the employee, and ultimately placed her in contact with counsel for the plaintiff in the *Dacrey Northrup* action. A month later, the employee, represented by plaintiff's counsel in the *Dacrey Northrup* action, initiated her own lawsuit against respondents, entitled *Hainley v. BKM Total Office of California et al.*[4] (the "*Hainley* action").

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[4] Los Angeles Superior Court case No. BC258605.

In the meantime, in August 2001, the plaintiff in the *Dacrey Northrup* action made another below limits settlement demand. Appellants agreed to the settlement on the condition that respondents contribute to the settlement and provide a conditional release of any bad faith claim against appellants. Because appellants had refused to pay any of the legal expenses incurred in the defense of the *Dacrey Northrup* action, and would not settle without respondents' participation, respondents felt compelled to accede to appellants' demands, and the case settled.

Respondents then tendered the defense of the *Hainley* action to appellants. Again, appellants failed to timely respond to the tender. Ultimately, appellants refused to provide a defense and indemnification in the *Hainley* action, and refused to turn over the notes from appellants' interview with *Hainley* to assist in respondents' defense of the action. Subsequently, appellants rejected tenders by respondents of other claims for defense and indemnification that were made during an extended reporting period that should have been afforded to respondents under the Policy.

Appellants' Motion to Compel Arbitration.

Respondents filed their complaint in the instant action on September 26, 2003. On December 23, 2003, appellants filed a motion to compel arbitration pursuant to section 2860, subdivision (c), a motion to stay proceedings, and a demurrer. On January 28, 2004 the trial court overruled the demurrer and denied both motions, ruling as follows: "The MOTION TO COMPEL arbitration is denied. This is not a dispute about billing rates. It is a case about bad faith, negligent misrepresentation, breach of the duty to defend and breach of a fiduciary duty. Civil Code Section 2860 does not cover these factual scenarios. (*Fireman's Fund Ins. [Companies v.] Younesi* (1996) 48 CA4th 451, 459.)"

Appellants appeal the denial of the motion to compel arbitration.

DISCUSSION

A. Appealability and Standard of Review.

An order denying a petition to compel arbitration is an appealable order. (*Fireman's Fund Ins. Companies v. Younesi* (1996) 48 Cal.App.4th 451, 456-457 (*Younesi*); Code Civ. Proc., § 1294, subd. (a).) This appeal raises the issue of whether section 2860, subdivision (c) requires arbitration of the claims set forth in respondents' complaint. We review the trial court's denial of the motion to compel arbitration de novo, because the trial court was not called upon to resolve any factual disputes, and lacked discretion to deny the motion under the terms of the statute if the complaint had presented a dispute over the amount of attorney fees owed to *Cumis* counsel. (*Gray Cary Ware & Freidenrich v. Vigilant Insurance Co.* (2004) 114 Cal.App.4th 1185, 1190; *Mitchell v. American Fair Credit Assn.* (2002) 99 Cal.App.4th 1345, 1350.)

B. Respondents' Claims Are Not Subject to Arbitration Under Section 2860, Subdivision (c).

Appellants contend that to the extent respondents' claims in this case constitute a dispute over appellants' alleged refusal to pay defense fees over a specific maximum hourly rate, the complaint is subject to arbitration under section 2860, subdivision (c).[5] We disagree.

Section 2860 "'deals with various aspects of an insured's selection of independent counsel where a conflict of interest has arisen between an insurer and its insured concerning the duty of the former to defend and indemnify the latter in litigation

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[5] Subdivision (c) provides in relevant part: "This subdivision does not invalidate other different or additional policy provisions pertaining to attorney's fees or providing for methods of settlement of disputes concerning those fees. Any dispute concerning attorney's fees not resolved by these methods shall be resolved by final and binding arbitration by a single neutral arbitrator selected by the parties to the dispute." (§ 2860, subd. (c).)

prosecuted by third parties. Where insurer and insured unconditionally agree independent counsel is warranted and where independent counsel is actually retained, subdivision (c) provides a simple remedy for resolving disputes concerning the fees to be paid to that individual or firm: arbitration.'" (*Handy v. First Interstate Bank* (1993) 13 Cal.App.4th 917, 925, quoting *Truck Ins. Exchange v. Dynamic Concepts, Inc.* (1992) 9 Cal.App.4th 1147, 1150-1151.)

Subdivision (c) of section 2860 has been uniformly interpreted to compel arbitration only in cases where the amount of legal fees or the hourly billing rate of independent counsel is in dispute. (See *Gray Cary Ware & Freidenrich v. Vigilant Insurance Co.*, *supra*, 114 Cal.App.4th at p. 1192.) Where the dispute centers on matters beyond the scope of a fee dispute, courts have refused to require arbitration pursuant to section 2860, subdivision (c). (See, e.g., *Truck Ins. Exchange v. Superior Court* (1996) 51 Cal.App.4th 985, 998 [disputes regarding an insurer's duties to defend and indemnify]; *Handy v. First Interstate Bank, supra,* 13 Cal.App.4th at pp. 923-924, 926 [disputes concerning scope of coverage, existence of a conflict of interest, duty to defend, and apportionment of attorney fees between insurers]; *Younesi, supra,* 48 Cal.App.4th at pp. 457- 459 [alleged fraud and malpractice of independent counsel]; *Caiafa Prof. Law Corp. v. State Farm Fire & Cas. Co.* (1993) 15 Cal.App.4th 800, 806 [alleged fraud and conspiracy to defraud under RICO statutes]; *Truck Ins. Exchange v. Dynamic Concepts, Inc., supra,* 9 Cal.App.4th 1147, 1150 [dispute between insurer and insured concerning duty to provide independent counsel at all].)

Furthermore, the provisions of section 2860 have been held to be inapplicable "in the absence of a stipulation or unconditional agreement between the insurer and insured, unless and until there has been a judicial determination of an insurer's duty to defend and the existence of a conflict of interest." (*Handy v. First Interstate Bank, supra*, 13 Cal.App.4th at p. 925; see also *Truck Ins. Exchange v. Dynamic Concepts, Inc., supra*, 9 Cal.App.4th at pp. 1150-1151.)

In *Younesi*, the request for arbitration was denied because the plaintiff had alleged a fraud claim in what would otherwise have been a simple billing dispute. (*Younesi, supra,* 48 Cal.App.4th at pp. 457-458.) The court held that "the language of Civil Code section 2860 can only be interpreted to limit the scope of arbitrable disputes to those in which only the amount of legal fees or the hourly billing rates are at issue." (*Id.* at p. 459.) Although the court found attorney billings to be a central issue in the case, it determined that the case was "not merely a dispute about billing rates," and concluded that the insurer's allegations of fraud, malpractice and conversion against *Cumis* counsel necessitated a jury trial. (*Younesi, supra,* at p. 458.)

So it is in this case. We reject appellants' attempt to characterize respondents' claims as a simple dispute over appellants' alleged refusal to pay the amount of attorney fees respondents had demanded. In support of their position, appellants claim the complaint is "rife with" allegations concerning fee disputes, pointing to various references in the complaint to Pacific's alleged failure to pay legal fees and costs. But nowhere in the complaint do respondents allege that the *amount* of legal fees or counsel's *billing rate* was in dispute. Rather, all of the allegations concerning legal fees pertain to appellants' failure to pay them at all. Moreover, an examination of the allegations concerning attorney fees reveals that, in each instance, the failure to pay attorney fees is alleged as part of a litany of malfeasance asserted against appellants, and evidence of appellants' bad faith. Under any fair reading of the complaint, it is clear that neither the amount of legal fees nor the hourly billing rates of *Cumis* counsel is a central issue in this bad faith action by an insured against its insurer.

Appellants seek to distinguish *Younesi* on the ground that the case did not involve an attorney fee dispute between insured and insurer, but was a lawsuit brought by the insurer against the insured's attorney for fraud and malpractice. But the absence of the insured as a party played no part in the *Younesi* court's interpretation of section 2860, subdivision (c) and its conclusion that only disputes over the amount of legal fees and

hourly billing rates are subject to arbitration. (*Younesi, supra*, 48 Cal.App.4th at pp. 458-459.)

Appellants further assert that respondents should not be able to circumvent the policy favoring arbitration of fee disputes by artful pleading that melds claims subject to arbitration with other claims that are not. The *Younesi* court rejected a similar argument with respect to artful pleading to avoid arbitration: "It is not an easy matter to simply add 'a magic' fraud cause of action. Fraud is not a cause of action which is 'magically added' and rarely disputed. Fraud requires that specific facts be pled and they are commonly contested by demurrer. Pleadings which allege causes of action which may lead to punitive and exemplary damages are nearly always strenuously opposed by party litigants. Moreover, if there is a legitimate basis to assert a claim for fraud it cannot be dismissed as a simple 'magic' tactic. If the claim is not legitimate that will be demonstrated at trial, producing adverse consequences for the claimant." (*Younesi, supra,* 48 Cal.App.4th at p. 458.)

In this case, none of the causes of action in respondents' complaint appears to have been "magically added" as embellishment to a fee dispute otherwise subject to arbitration. Indeed, even if the attorney fees allegations were removed, each of the causes of action alleged in the complaint would still state a viable claim for relief.

Finally, appellants contend that enforcing the plain language of section 2860 to compel arbitration in this case would serve the strong public policy in California favoring arbitration. (See *Aguilar v. Lerner* (2004) 32 Cal.4th 974, 983.) But appellants have not shown how any public policy would be served by compelling arbitration of claims that clearly fall outside the scope of arbitrable claims as contemplated by section 2860. "While arbitration is currently viewed as an efficient and favored method of dispute resolution, without a statutory mandate or contractual provision requiring its use, a litigant cannot be deprived of its day in court." (*Truck Ins. Exchange v. Dynamic Concepts, Inc., supra*, 9 Cal.App.4th at pp. 1150-1151.)

DISPOSITION

The order is affirmed. Appellants to bear respondents' costs of appeal.

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_____, J.

DOI TODD

We concur:

_____, Acting P. J.

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_____, J.

ASHMANN-GERST